VZCZCXRO8448
RR RUEHAG RUEHCHI RUEHDF RUEHFK RUEHHM RUEHIK RUEHKSO RUEHLZ RUEHNAG
RUEHPB RUEHRN RUEHROV
DE RUEHWL #0115/01 0901858
ZNR UUUUU ZZH
R 301858Z MAR 08
FM AMEMBASSY WELLINGTON
TO RUEHC/SECSTATE WASHDC 5167
RUEHRC/DEPT OF AGRICULTURE WASHDC
RUCNMEM/EU MEMBER STATES COLLECTIVE
RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION
RUEHSS/OECD POSTS COLLECTIVE
RUEHNZ/AMCONSUL AUCKLAND 1647
RUEHDN/AMCONSUL SYDNEY 0657
RUCPDOC/USDOC WASHDC 0218
RUEAWJA/DEPT OF JUSTICE WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHDC
RUEHRC/USDA FAS WASHDC 0383
RUEHBS/USEU BRUSSELS

UNCLAS SECTION 01 OF 02 WELLINGTON 000115

SIPDIS

SIPDIS

SENSITIVE

STATE FOR EAP/ANP, EEB/TPP/ABT, STATE PASS TO FAS KHALIKA MEARDY
OCRA, PAUL KIENDL OGA, JIM DEVER OFSO, COMMERCE FORITA/MAC/AP/OSAO,
PACOM FOR JO1E/J2/J233/J5/SJFHQSTATE

E.O. 12958: N/A
TAGS: EAGR ECON EFIN ETRD PREL NZ XV
SUBJECT: NO TURNING BACK THE SUBSIDY CLOCK FOR NEW ZEALAND FARMERS

WELLINGTON 00000115 001.2 OF 002

¶1. Note: This is a joint Foreign Agricultural Service and State report. End note.

¶2. (SBU) Summary. Up until approximately twenty years ago, New Zealand farmers were some of the most heavily subsidized in the world. Farmers were provided with price supports, low-interest loans, extensive disaster relief, weed-eradication subsidies and special training programs. However, as the level of farm support grew, it became an increasingly impossible financial burden for the country to bear and agricultural subsidies, which represented as much as 33% of farm income, were eliminated in 1984. Although the transition to an unsubsidized farm economy wasn't easy, agriculture has maintained its crucial place in the New Zealand economy accounting for approximately 5% of gross domestic product (GDP) and over 55% of merchandise exports. The acceptance of subsidy-free agriculture is now firmly entrenched in New Zealand's psyche, a view supported by the country's largest farm lobby. There is no call by New Zealand farmers to turn the clock back. End summary.

## Agricultural Deregulation Pays Off

¶3. (SBU) By most accounts, New Zealand's experimentation with agricultural deregulation is a major success story. The percentage of the GDP accounted for by agriculture is holding its own at 5%. Farm productivity is increasing annually by 3.4%, on average, compared with 0.5% in subsidy days. Land values are soaring. Agricultural exports are strong accounting for over 55% of merchandise exports. New Zealand, which exports most of what is produces, is the world's largest exporter of dairy products, sheep meat, venison and kiwifruit and the second largest exporter of wool.

## Rural Economy Changed as a Result

¶4. (SBU) Deregulation altered the landscape of New Zealand agriculture with dairy, rather than sheep and beef, emerging as the largest sub sector making up approximately one third of the

country's commodity exports. Fonterra, the largest dairy cooperative in New Zealand with a 95% share of the domestic production, has a 40% share of world trade in dairy products. In response to high international dairy prices, Fonterra hiked its domestic payout to dairy farmers to a record NZ $6.90 (US $5.31) per kilogram of milk solids. This represents a 58.6% jump from last year and equals an estimated NZ $3 billion (US $2.4 billion) increase in dairy farmer revenues (although costs have also gone up). Over the next few years, New Zealand dairy production is expected to increase faster than in previous years as more land is being converted to dairying, especially in the Southland and Canterbury regions of the South Island. Along with dairy, horticultural production has also increased in importance with horticultural exports, including wine, expanding by a factor of 10 since 1984. Wine is a particular standout. The total area planted in wine grapes increased to 29,680 hectares in 2007, up 23% since ¶2005. Wine exports are expected to overtake kiwifruit exports, on a value basis, in 2008.

Yet Some Sectors Falling on Harder Times
----------------------------------------

¶5. (SBU) While wine exports are breaking records and dairy farms are selling at record prices (median price per hectare is NZ $37,000 or US $29,600), sheep producers have fallen on hard times. With poor returns, increasing on-farm costs (shearing and fertilizer), high capital costs (land), and an over supply of sheep meat on world markets, there is a strong negative sentiment among farmers about the future profitability of sheep. The problems besetting sheep farmers have been amplified by drought conditions over much of the country. Some farmers on the east coast of the North Island and parts of the South Island are now in their second summer of drought and water shortages are taking their toll. A report from the Ministry of Agriculture and Forestry found the drought's cost was NZ $345 million (US $276 million) for sheep and beef farmers - or NZ $25,200 (US $20,160) for the average sheep and beef farm. Real farm profit for sheep and beef farmers has dropped significantly from NZ $66,800 (US $53,440) in 2003-04 to NZ $38,700 (US $30,960) in



2006-07 and is forecast by Meat and Wool New Zealand, an industry organization, to fall to NZ $19,543 (US $15,634) in 2007-08, assuming the New Zealand dollar stays in the US $0.80 range. The exchange rate is a big factor impacting on all New Zealand farmers. For sheep farmers, the record high New Zealand dollar is wiping out the benefits from better market prices. Wool market prices from July 2007 to December 2007 were up 3.7% and lamb prices were up 8% but the exchange rate appreciated 7.9%. Market prices for beef in North America, New Zealand's largest market, are reportedly at near historical highs but, when converted to New Zealand dollars, prices are down 10%. According to industry analysts, if the exchange rate stays at its current high level, this would make for the third worst year for the sheep and beef industry in 50 years, which is in stark contrast to the dairy industry.

Farmers Not Calling for Return to Old Ways
------------------------------------------

¶6. (SBU) In spite of the difficult times facing sheep producers in New Zealand, farmers are not calling for a return to subsidies. Instead, many see a fragmented meat marketing structure as a big part of the problem. Alliance, one of two major meat processing cooperatives, has proposed a merger with other processors and is currently soliciting farmer reaction to the idea. The mega meat company would have an 80% share of New Zealand's livestock supply and would require approval from the New Zealand Government.

¶7. (SBU) Over the last two decades, the New Zealand agricultural economy has gone from being one of the most heavily subsidized in the world to having by far the lowest level of producer support in the Organization for Economic Cooperation and Development. In spite of drought conditions and poor returns, a mindset characterized by hardy independence is now deeply ingrained in New Zealand farmers. Most farmers would not want to return to subsidies because, in their view, it would put New Zealand agriculture at a competitive disadvantage by blocking market signals, increasing inefficient production and discouraging innovation.

Farm Lobby neither Wants nor Expects Govt Helping Hand
---------------------------------------------- ---------

¶8. (SBU) The resilient independence of the NZ farmer was upheld by Annabel Young, Chief Executive of Federated Farmers, New Zealand's largest and most influential farming lobby. In a conversation with Post, Young said that her organization has not sought any rural assistance package from the Government in this year's budget, nor does she expect any. Young noted that the Government is extremely reticent about rendering assistance to farmers. Even in the event of natural disasters, Young said that any specific government assistance for affected rural areas is usually limited to the restoration of vital infrastructure. Consequential loss of income and insurable assets are not covered by the Government. Farmers are able to receive work and income assistance ("welfare") payments in the case of hardship, but this is no different from any other welfare recipient in New Zealand.

McCormick